

**Statement of Steve Chabot,
Chairman, Committee on Small Business
Before the Committee on Armed Services of the House of Representatives
On the FY 2016 National Defense Authorization Act
April 14, 2015**

Good morning, Chairman Thornberry, Ranking Member Smith, and Members of the Committee. I appreciate the opportunity to testify before you on the National Defense Authorization Act for Fiscal Year 2016 (FY16 NDAA). Let me begin by thanking the Committee for its longstanding collaboration with the Small Business Committee. In my 19 years on the Small Business Committee, I've enjoyed seeing this relationship develop, and in my first year as Chairman, I hope to continue the tradition. My testimony today will first address the Committee's current work on contracting, then discuss the Small Business Committee's contracting legislation this Congress, and will conclude with two other provisions worthy of the Committee's consideration.

I. H.R. 1597

I want to compliment Chairman Thornberry and Ranking Member Smith on H.R. 1597, the Agile Acquisition to Retain Technological Edge Act. H.R. 1597 has many provisions that will help our small business technological and industrial base. I think that many of the provisions in H.R. 1597 will help small businesses, and I hope that you will include them in the FY16 NDAA. Specifically, I hope that the Committee will incorporate the following ten provisions from H.R. 1597 in the NDAA:

1. *Sec. 501. Codification and amendment of Mentor-Protégé Program.* Providing permanency to this long running program will give greater certainty to small protégés, and their mentor firms. However, the Committee should consider expanding the pool of potential protégés to include small businesses, not just small disadvantaged businesses, women-owned small businesses, service-disabled veteran-owned small businesses, and qualified HUBZone firms. The Small Business Committee has a long standing policy of promoting parity between each of the small business programs, and would encourage this Committee to apply those principles of parity to the mentor-protégé program.
2. *Sec. 502. Amendments to data quality improvement plan.* Contract bundling and consolidation continue to be the top complaint of small contractors. When bundling and consolidation are unjustified, it restricts competition without providing a measurable benefit to offset the loss of opportunity. Consequently, since 1997 the Small Business Act (the Act) has required that federal agencies justify the decision to bundle contracts, and take the appropriate steps to mitigate that decision. Unfortunately, eighteen years after the Act was amended, agencies continue to fail to simply identify contracts as bundled. This provision will require the federal government to implement a plan to improve the quality of bundling and consolidation data.
3. *Sec. 503. Notice of contract consolidation for acquisition strategies.* Small businesses are permitted to challenge bundling and consolidation at the Government Accountability Office. However, since consolidation and bundling justifications need not be published for a year after the award of the contract, it makes it impossible for small businesses to

challenge the underlying merits of the decision. This provision solves that problem by requiring agencies to publish justifications concurrent with the solicitation.

4. *Sec. 504. Clarification of requirements related to small business contracts for services.* The Nonmanufacturer Rule (NMR) was always envisioned by Congress, and interpreted by the Small Business Administration (SBA), as a protection against front companies when contracts for goods were restricted to small businesses. In the case where a contract is set aside for small businesses, the government has a vested interest in the small business actually performing the work, or manufacturing the goods, so various limitations on subcontracting are codified in the Act. However, some small manufacturers sell through other small businesses, or incorporate the product of another small business when fulfilling orders for multiple different items. For that reason, the NMR was created – it requires that when a small business accepts a set-aside contract for goods, the small business either manufacture the product, purchase the product from another small manufacturer, or obtain a waiver. This keeps small businesses from receiving contracts and then simply reselling goods from a large manufacturer. Unfortunately, the Court of Federal Claims has begun applying the NMR to service contracts. SBA and the Committee on Small Business both agree that this is inappropriate, and does not protect the government against fraud. This provision will preserve the long standing interpretation of the NMR.
5. *Sec. 505. Review of Government access to intellectual property rights of private sector firms.* According the SBA Office of Advocacy (Advocacy), of high patenting firms (15 or more patents in a four year period), small businesses produced 16 times more patents per employee than large patenting firms. However, the government's arcane approach to intellectual property rights often acts as a barrier to entry for small businesses. Thus, any improvements in the current system would be welcome.
6. *Sec. 507. Extension of defense research and development rapid innovation program.* I applaud the effort to extend the Defense Research and Rapid Innovation for another five years. This program, which has existed for five years, successfully allows innovative companies to quickly meet the Department of Defense's critical needs.
7. *Sec. 704. FAR Council membership for Administrator of Small Business Administration.* The SBA plays an important role in the procurement process. The SBA's rules govern nearly \$100 billion in prime contracting each year, and another \$300 billion in subcontracting. This is more than the General Services Administration and the National Aeronautics and Space Administration combined. However, regulations governing these dollars are bifurcated into both the SBA's regulations in chapter 13 of the Code of Federal Regulations, and the Federal Acquisition Regulation (FAR). This means that when Congress passes laws regarding small business contracting, SBA must publish a proposed regulation, followed by a final regulation, then the FAR Council publishes a proposed regulation, and then a final regulation. This process is time consuming, unwieldy, and results in conflicting rules. For example, Congress passed small business procurement reforms as part of the Jobs Act of 2010, the FY13 NDAA, FY14, NDAA, and FY15 NDAA. While some of the reforms from the 2010 law have been

implemented, many are still outstanding five years later. One change from the FY13 NDAA has been implemented by both agencies, but the rest are still pending. At this pace, the final rules from the FY13 NDAA should be implemented in late 2018 or early 2019. These delays force small businesses and contracting officers to deal with conflicting regulations that do not reflect the actual state of the law, and to incur huge compliance burdens. When the final rules are ultimately implemented, the dual rulemaking process results in conflict between chapter 13 and the FAR. Incorporating SBA into the FAR Council will streamline this process, but also provide industry with a stronger voice in the rulemaking process, as SBA is likely to be more concerned with compliance burdens on contractors than other agencies.

8. *Sec. 705. Independent study of matters related to bid protests.* Bid protests remain an item of consternation for small businesses. While there were 2,561 bid protests last year, that number should be seen in context – there are over 300,000 companies registered to business with the federal government, and there were over 15 million contract actions during that period. While there are certainly abuses of the protest process, there are also reports from many small businesses that they will not protest over fears of retribution from contracting agencies. I hope that the study and recommendations will help ensure that neither the protest process nor the meritorious protestor are abused.
9. *Sec. 706. Procurement of commercial items.* As many small businesses sell commercial goods and services, any effort to streamline the process by which an item is considered a “commercial item” will reduce the burden on those small contractors. The current process acts as a barrier to entry for many innovative companies, which in turn means that the federal customer does not always have access to the best available solution.
10. *Sec. 710. Amendments to certain acquisition thresholds.* Increasing the simplified acquisition threshold will relieve many small businesses of unnecessary compliance burdens, while also making it easier for the government to competitively contract for routine goods and services. It is expected that this will make it easier for new government contractors to access the federal marketplace.

I believe that all of these provisions will enhance the federal procurement process, and I again commend you for this effort.

II. H.R. 1481

In addition to H.R. 1597, I believe there are other common sense reforms we can work on together. As you know, the federal government spends nearly half a trillion dollars through prime contracts each year. Ensuring that small businesses can compete for these contracts offers several benefits – business growth, job creation, greater competition, lower prices, and innovation. Over the past few months, the Small Business Committee has held three hearings on small businesses in the industrial base. I’d like to briefly share our findings, which led to the introduction of H.R. 1481, the Small Contractors Increase Competition Act of 2015.

As discussed at hearings on February 12, 2015, March 17, 2015, and March 19, 2015, the Small Business Committee is concerned that the small business goaling process is being misused to the detriment of small businesses, and is giving an inaccurate view of the health of the small business industrial and technological base. Under the SBA's scorecard system, the federal government received an "A" grade for FY 2013.¹ While an "A" grade and a reasonable percentage of small business prime contracting dollars would seem to indicate that a healthy percentage of dollars are being awarded to small businesses, it is not reasonable when Chart 1 shows that the use of small businesses is declining even as the percentage of dollars awarded to small businesses increases. Additionally, it is worth noting that in obtaining its A, the federal government did not meet half of its numerical goals.²

Chart 1. Small Business Contracting FY10-FY14³

FY	Total Contract Dollars (in Billions)	Total Small Business Dollars (SB)	Total Number of SB Actions	Total DoD Contract Dollars	Total DoD Small Business Dollars	Total Number of DoD SB Actions	Average Value of Small Business Contract Action	Average Value of Small Business Contract Action
11	\$549.6	\$103.6	3,346,553	\$374.1	\$60.4	2,325,622	\$30,957.23	\$25,971.55
12	\$518.3	\$100.0	2,584,893	\$290.1	\$60.2	1,453,952	\$38,686.32	\$41,404.39
13	\$462.3	\$91.9	1,560,467	\$308.5	\$50.0	711,998	\$58,892.63	\$70,224.92
14	\$444.7	\$98.9	1,390,987	\$284.7	\$55.6	745,626	\$71,100.59	\$74,568.22

From FY11 through FY14, the percentage of dollars awarded to small businesses increased each year, from just over 18 percent to approximately 22.25 percent.⁴ At the same time, despite a decline in overall federal spending, the dollars awarded to small businesses remained fairly constant during this period. While this would normally be heralded as a success, a deeper dive into the numbers shows that the number of small business contract actions fell by almost 60 percent and the average size of a contract action increased 230 percent. This reflects that fewer small businesses are winning contracts, but those contracts are worth more, which may indicate

¹ SBA, "FY 2013 Procurement Scorecard," available at https://www.sba.gov/sites/default/files/files/FY13_Government-Wide_SB_Procurement_Scorecard_Public_View_2014-04-28.pdf (last accessed February 26, 2015).

² SBA, "FY 2013 Procurement Scorecard," available at https://www.sba.gov/sites/default/files/files/FY13_Government-Wide_SB_Procurement_Scorecard_Public_View_2014-04-28.pdf.

³ *Id.*

⁴ Analysis based upon FPDS, available at <https://www.fpds.gov> (last accessed January 28, 2015). Copies of reports are on file with the Committee.

that some small businesses are doing very well but many others are losing opportunities to compete.

Alarmingly, at the Department of Defense (DoD), which is arguably a better reflection of the federal government's ability to maintain a healthy industrial base capable of supporting defense programs, the results were worse. The percentage of contract dollars awarded to small businesses at DoD increased from just over 16 percent to just over 19 percent, but the actual dollars only fluctuated by about 10 percent. The number of small business contract actions at DoD fell by almost 70 percent, and the value of those contract actions rose by nearly 290 percent.

The declining number of contract actions with small businesses cannot simply be explained by shrinking budgets or sequestration, because during the same period, the number of contract actions with large businesses increased by 8 percent. However, the dollar value of the average contract action with a small business increased 230 percent, meaning that fewer small companies are getting contracts, but the contracts they get are getting much bigger.

Furthermore, the number of companies registered to do business with the federal government has dropped by over 100,000 from 2012, so that only 273,072 small businesses are still registered to compete for federal contract.⁵ This speaks to a greater problem in the industrial base—a declining participation rate.

SBA Advocacy recently highlighted this small business participation problem. Specifically, Advocacy identified 23 industries in which the government spends over \$500 million per year, but where less than 10 percent of procurements are awarded to small businesses.⁶ These are areas important to the industrial base where small businesses are not participating, but this is not reflected in the current scorecard process.

Consequently, I recommend three legislative changes to the small business goaling process, each of which is included in H.R. 1481. I strongly encourage you to include each of the following three provisions, identified by their section in H.R. 1481, in the FY16 NDAA.

1. *Sec. 101. Amendment to Governmentwide goal for small business participation in procurement contracts.* This section requires that SBA work to increase the number of industries in which small businesses compete for contracts. Currently, there are gaps in our industrial base but no policy of encouraging small businesses to compete for work in these areas, which exacerbates the problem and leads to less competition and higher prices.

⁵ Data retrieved from the System for Award Management, available at www.sam.gov (last accessed January 28, 2015). This number is down by over 100,000 small businesses from 2012, when DSBS reported 382,092 active small businesses.

⁶ SBA Advocacy, EVALUATION OF THE SMALL BUSINESS PROCUREMENT GOALS ESTABLISHED IN SECTION 15(G) OF THE SMALL BUSINESS ACT 41-42 (2014).

2. *Sec. 102. Including subcontracting goals in agency responsibilities.* Currently, when considering whether senior agency executives are eligible for bonuses, agencies must look at whether they met the small business prime contracting goals. However, agencies don't look at whether the agency is meeting its subcontracting goals. As a consequence, the percentage of subcontract dollars awarded to small businesses has been falling, and is down 2.5% since 2010. Make no mistake about the significance of subcontracting: in FY 2013, small businesses received \$86.7 billion in subcontracts. Subcontracting is an important entry point for federal contractors. Therefore, this provision holds senior agency officials accountable for meeting all the goals.
3. *Sec. 103. Scorecard program for evaluating Federal agency compliance with small business contracting goals.* This provision redirects SBA's scorecard program. Currently the program allows SBA to award "A" and "A+" grades to agencies that fail to meet the goals. As implemented now, only 10 percent of an agency's grade looks at its subcontracting achievements, even though if all the goals had been met in FY 2013, prime contracting would have only accounted for 0.001 percent more dollars than subcontracting.

This legislation would require that SBA look at all five prime contracting goals, all five subcontracting goals, grades, the number of each type of small businesses awarded contracts in each industry each year, and the number of each type of small businesses competing for contracts in each industry each year. Thus, while it still would place a premium on dollars awarded to small business prime contractors, it would also encourage a greater small business participation rate to increase competition and improve the health of the industrial base.

In addition to the Small Business Committee's work on goaling, we also examined procurement practices that inhibit small business competition. As discussed at hearings on February 12, 2015, March 17, 2015, and March 19, 2015, the Small Business Committee is concerned that current procurement practices are limiting the ability of small businesses to compete and thereby undermining the federal procurement process. While H.R. 1597 addresses many of these, I would also request that you include two additional provisions:

1. *Sec. 301. Joint venturing and teaming.* The Act encourages small businesses to team and joint venture, and the SBA will approve joint ventures to facilitate small businesses participating on federal contracts. In the 112th Congress, this Committee successfully passed legislation as part of the National Defense Authorization Act for FY 2013 to make it easier for small businesses to team by changing the limitations on subcontracting. However, small businesses that do team and joint venture are often unsuccessful at winning contracts because some agencies have stated that the agency will only consider the past performance or financial responsibility of the joint venture or the prime contractor, not the small business members of the joint venture or the parties to the team.

As many joint ventures are never populated – especially small business joint ventures – this all but disqualifies the small business from competition. This provision requires that contracting officers look at the qualifications of team members and members of the joint venture.

2. *Sec. 302. Restrictions on reverse auctions.* As defined by this provision, reverse auctions are an auction between a group of offerors who compete against each other by submitting offers for requirement, and offerors have the ability to submit revised offers with lower prices throughout the course of the auction. When used properly, reverse auctions are an important tool that may benefit taxpayers and contracting agencies. However, when used inappropriately, reverse auctions may place taxpayers, warfighters and small businesses at risk. GAO has issued reports calling for reforms of the reverse auction process, and two bid protests have been sustained this month because of abuses of reverse auctions. Therefore, this language creates a new section of the Act to limit the use of reverse auctions when using small business contracting authorities. Specifically, it requires training of contracting officers, and prohibits the use of reverse auctions for sole source contracts or contracts with inadequate competition. It also states that reverse auctions should only be used when the good or service being purchased can be considered only either technically acceptable or unacceptable. This provision requires that the government communicate honestly with bidders regarding the ranking of offers, as some reverse auctions have misled offerors regarding the status of bids. The bill also makes it clear that when using a third-party reverse auction service, the government must still follow all of the normal procurement rules, as there are cases where a third party provider is excluding companies from competing or using third party data to inform responsibility determinations. Finally, the provision states that reverse auctions may only be used for contracts other than contracts for construction, goods used to protect people from bodily harm, and technical goods and services.

Finally, in an effort to operate more efficiently, SBA has suggested that the following changes would allow it to save money and better serve taxpayers:

1. *Sec. 402. Training requirements for Procurement Center Representatives.* SBA's Procurement Center Representatives (PCRs) act as advocates for small contractors within federal agencies. Current law requires that PCRs have the highest level federal contracting certification, making it difficult to hire qualified individuals in some areas without incurring relocation expenses. This provision gives SBA one year from the date of hire to train the PCRs.
2. *Sec. 403. Training requirements for Business Opportunity Specialists.* SBA's Business Opportunity Specialists (BOS) work with small contractors in the district offices. Current law requires that BOSs have an entry level federal contracting certification, making it difficult to hire qualified individuals in some areas without incurring relocation

expenses. This provision gives SBA one year from the date of hire to train the BOSs. At the suggestion of the Small Business Committee's Ranking Member Nydia Velázquez, I would further suggest expanding this provision to cover Commercial Market Representatives.

The Small Business Committee has received testimony supporting provisions of the bill from the American Council of Engineering Companies, Mechanical Contractors Association, Women Impacting Public Policy, Veterans Entrepreneurship Task Force, the American Legion, and the Professional Services Council. The bill has also been endorsed by the National Defense Industrial Association, Mid Tier Advocacy, Associated General Contractors, the American Institute of Architects, and the National Electrical Contractors Association. H.R. 1481 was successfully marked up and reported with bipartisan support on March 25.

III. Other Considerations

In addition to H.R. 1597 and H.R. 1481, I'd ask the Committee to include H.R. 838, the Security in Bonding Act of 2015, and H.R. 1666, the Design Build Efficiency and Jobs Act of 2015 in the FY 16 NDAA. H.R. 838 is a no-cost provision that makes it easier for small businesses to obtain mandatory surety bonds. This legislation also requires that the surety bond presented to the government have the assets to back the bond, which decreases the risk for taxpayers.

H.R. 1666 seeks to reform the design-build contracting process. The current process is so cost intensive that many qualified companies forgo the federal marketplace entirely. H.R. 1666 simplifies the process, reducing the amount of paperwork initially required from contractors, while also alleviating the workload on contracting officers. This implements a best practice already successfully used by the Corps of Engineers, and applying this policy governmentwide is good for taxpayers, agencies, small businesses, and large businesses.

IV. Conclusion

In conclusion, I know that we agree that our nation deserves vital small business industrial base: it is fundamental to the health of our nation as a whole. I look forward to working with this Committee to ensure that small businesses remain continue to provide the Department of Defense and the federal government with innovative and competitive solutions to support critical programs. I'd be happy to answer any questions.